Franchise Tax Board

ANALYSIS OF ORIGINAL BILL

Author:	Nava	Analyst:	Nicole Kwon	Bill Number:	AB 164
Related Bills:	See Legislative History	Telephone:	845-7800	Introduced Date:	1-19-2005
		Attorney:	Patrick Kusiak	Sponsor:	

SUBJECT: Disaster Loss Deduction/Excess Loss Carryover/Santa Barbara & Ventura County Severe Rainstorms, Related Flooding, Slides, & Other Events

SUMMARY

This bill would allow taxpayers special tax treatment, called disaster loss treatment, for losses sustained as a result of the severe rainstorms and related events that occurred in Santa Barbara and Ventura Counties.

This analysis will not address the bill's changes to the Property Tax Law as they do not impact the department or state income tax revenue.

PURPOSE OF THE BILL

According to the author's office, the purpose of the bill is to provide immediate tax relief to individuals and businesses affected by the severe rainstorms and related events in Santa Barbara and Ventura Counties.

EFFECTIVE/OPERATIVE DATE

As introduced, this bill is an urgency statute and would be effective and operative immediately.

POSITION

Pending.

ANALYSIS

FEDERAL/STATE LAW

Under federal and state law, a disaster loss occurs when property is destroyed as a result of a fire, storm, flood, or other natural event in an area proclaimed to be a disaster by the President of the United States or, for state law purposes, by the Governor.

Under federal and state tax law, the taxpayer may elect to claim the loss either in the year the loss occurs or in the year preceding the loss. This election allows the taxpayer to file an amended return immediately for the prior year. For state purposes, this election may be made for any Presidentially-declared disaster prior to passage of any state legislation allowing special carryover treatment because California conforms to federal law. The election is available for a Governor-only declared disaster only if enabling legislation is enacted.

Board Position:			Department Director	Date
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A nonbusiness disaster loss not reimbursed by insurance or otherwise is deductible under both state and federal tax law to the extent of two limitations: basis limitation and adjusted gross income limitation. Under the basis limitation, a nonbusiness disaster loss is deductible to the extent the loss exceeds $100. Under the adjusted gross income limitation, total nonbusiness disaster losses are deductible only to the extent that the total loss amount for the year exceeds 10% of adjusted gross income.

State tax law identifies specific events as disasters that are then allowed additional special loss carry over treatment. That is, 100% of the excess disaster loss may be carried over for up to five taxable years, and if any excess loss remains after the five-year period, the remaining loss may be carried over at a specified percentage for up to 10 additional years.

BACKGROUND

Governor Schwarzenegger proclaimed a disaster due to the severe rainstorms and related events in Ventura County on January 12, 2005, and in Riverside, Santa Barbara, Los Angeles, Kern, San Bernardino, Orange, and San Diego Counties on January 15, 2005. On February 4, 2005, President Bush declared a disaster in the above counties.

THIS BILL

This bill would add the severe rainstorms and related events that occurred in Santa Barbara and Ventura Counties in December of 2004 and January of 2005 to the current list of specified disasters under the Personal Income Tax Law (PITL) and the Corporation Tax Law (CTL).

Specifically, this bill would allow special disaster loss carry over treatment of losses sustained as a result of those disasters in those counties. The $100 and 10% of adjusted gross income limitations in existing law would apply to disaster losses on nonbusiness property.

Due to President Bush's disaster declaration for Santa Barbara and Ventura Counties, this bill would allow the taxpayer to elect to claim the loss either in the year the loss occurred or in the year preceding the loss.

IMPLEMENTATION CONSIDERATIONS

Once the technical consideration discussed below is resolved, implementing this bill would not significantly impact the department's programs and operations.

TECHNICAL CONSIDERATIONS

For consistency with other disaster provisions, the author may wish to remove "and related flooding, slides, and other events" on page 8, lines 34 and 35 and on page 11, lines 38 and 39, and replace it with "related flooding and slides, and other related casualties" to identify other events that were connected to and occurred as a result of the severe rainstorms.

LEGISLATIVE HISTORY

AB 1510 (Kehoe, Ch. 772, Stat. 2004) allows taxpayers disaster loss treatment for losses sustained as a result of the following disasters: Middle River levee break in San Joaquin County, Southern California wildfires, floods, mudflows, and debris flows directly related to the Southern California wildfires, and San Simeon earthquake.

AB 44 (Wiggins, Ch. 618, Stat. 2001) allowed taxpayers disaster loss tax treatment for losses sustained as a result of the earthquake that occurred September 2000 in Napa, California.

AB 18 (La Malfa, 2005/2006) would allow taxpayers disaster loss treatment for losses sustained as a result of the Shasta County wildfires.

OTHER STATES' INFORMATION

Michigan, Minnesota, Massachusetts, and *New York* conform to the federal provisions that allow taxpayers to claim a disaster loss deduction on their state returns either in the preceding year or in the year of the loss. It appears that legislation, executive order, or proclamation by the President or the Governor is required to identify the area impacted by a disaster that is eligible for federal or state assistance.

Florida does not have a personal income tax; however, monetary relief is provided to citizens and corporations through the Emergency Management, Preparedness, and Assistance Trust Fund. Florida also requires legislation, executive order, or proclamation to identify the area impacted by a disaster.

FISCAL IMPACT

This bill would not significantly impact the department's costs.

ECONOMIC IMPACT

<u>Revenue Estimate</u>

Estimated Revenue Impact Assumed Immediate Enactment Date Fiscal Year Impact		
2005-06	**2006-07**	**2007-08**
Insignificant	Insignificant	Insignificant

Insignificant = Loss of less than $150,000

This analysis does not consider the possible changes in employment, personal income, or gross state product that could result from this measure.

Revenue Discussion

Total property damages attributable to the 2005 Ventura County rainstorms are estimated at $75 million. Since data is not readily available for personal property damages in Santa Barbara County, it is assumed that the order of magnitude is similar to the damages reported by Ventura County. The estimate is based on $150 million in property damages.

Based on data provided by Ventura County, business losses represent approximately 65% of total losses and will not impact revenues since under current law, CTL already provides carryover loss provisions for business related losses.

The remaining 35% is attributable to personal property losses, resulting in approximately $52.5 million ($150 million x 35%) in losses for personal income tax (PIT) taxpayers.

Of the $52.5 million in total PIT losses, it is estimated that 90% of personal losses are insured. Therefore, uninsured losses are $5.25 million (52.5million x 10% = $5.25 million).

It is estimated that basis limitations will reduce losses for tax purposes by 1.5% of total PIT losses to $4.47 million ($5.25million - ($52.5 million x 1.5%=$0.78 million) = $4.47 million). Qualifying losses must further be reduced to reflect adjusted gross income limitations. It is estimated that this limitation represents 1.5% of total PIT losses and reduces the applicable losses to $3.69 million ($4.47 million. – ($52.5 million x 1.5%= $0.78 million) = $3.69 million).

Total losses of $3.69 million may be used in the year prior to the disaster, the year of the disaster, or carried forward to future years. It is estimated that 33% will be used during the year of the disaster and 5% will never be utilized. The other 62%, $2.28 million ($3.69 million x 62% = $2.28 million), will be carried forward and allowed for use in future years. Assuming an average marginal tax rate of 6%, this proposal's total revenue loss approximates $137,000 ($2.28 million x 6% = $137,000). If total losses of $137,000 are carried forward and utilized over a three-year period, the revenue impact is deemed as insignificant.

ARGUMENTS/POLICY CONCERNS

This bill would only allow taxpayers in Santa Barbara and Ventura Counties the special disaster loss carry forward treatment. Governor Schwarzenegger and President Bush proclaimed a disaster due to the severe rainstorms and related events to six other counties in Southern California. This bill would not apply to the following counties: Riverside, Los Angeles, Kern, San Bernardino, Orange, and San Diego.

LEGISLATIVE STAFF CONTACT

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